FISCAL FEDERALISM IN RUSSIA: RULES VERSUS ELECTORAL POLITICS*

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ABSTRACT

This paper examines the determinants of financial flows between the federal government and regional authorities in Russia. The main question is to what extent intergovernmental transfers correspond to the "ideal pattern" – equalization of the abilities of the regions to provide public goods – and to what extent, if at all, they reflect the influence of federal-regional political discourse (asymmetrical federalism). The main finding is that actual net transfers since 1994, although quite close to the "ideal patterns", depended also on the results of the parliamentary (1993, 1995, 1999) and presidential (1996, 2000) elections and on the relations of the regions with the federal center. The more votes cast for pro-central government parties in parliamentary elections and for Yeltsin in 1996 presidential elections and the lower the tensions with Moscow after the elections, the more favorable was the fiscal balance for the region with the federal center. The result is very robust when using different measures of fiscal capacity (index of tax potential) and costs of providing public goods (budgetary expenditure adjustment index).

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1. Review of the literature

The emergence of the system of fiscal federalism in Russia in recent years was one of the most important reforms in the public sector that was carried out during transition. Not surprisingly, there is a rapidly growing literature on this subject. With some reservations, it can be divided into three broad categories. *First,* there are normative papers that seek to put Russian experience into the international context and to design a system of equalization payments that is most appropriate for Russian conditions (Batkibekov, Kadotchnikov, Lugovoy, Sinel'nikov, Trounin, 2000; Lavrov, 2000; Martinez and Boex, 1997a,b,c, 1999; Morozov, 1999; Kadotchnikov, Lougovoi , Trounin, 1999; Trounin, 1999, Minfin, 2001). S*econd*, there are papers that examine the actual factors that affect intergovernmental transfers in the transition period (Freinkman and Haney, 1997; McAuley, 1997; Popov, 2001; Stewart, 1997; Tabata, 1998, 2000; Triesman, 1996, 1998a,b; Zhuravskaya, 2000). The main question discussed in these papers is to what extent actual transfers are really equalizing and to what extent they are used as an instrument of federal-regional politics (rewarding either pro-center governors or troublemakers). *Third*, there are studies of broader scope, mostly political science papers about the nature of Russian federalism that incorporate fiscal intergovernmental flows into a general model of center-regional relations and explain the decentralization or centralization tendencies in the Russian Federation that occurred during the 1990s and the behavior of regions and central authorities in the "bargaining federalism game". (Petrov, 2000; Polishchuk, 1998; Solnick, 1999; Speckhard, 2000; Stoner-Weiss, 2000.

This paper belongs to second steam of literature and seeks to identify economic and political factors affecting financial flows between the center and the regions in the 1990s and the early 2000s. Whereas there is a near-consensus that the Russian system of fiscal federalism in the

1990s was far from being perfect, there seems to be little agreement between scholars on what the key determinants of intergovernmental financial flows have been.

As documented by Triesman (1996 and 1998 a, b), financial transfers from the federal budget to the regions in 1992 and 1994 depended mostly on the lobbying power of the regions, which in turn was determined by their ability to threaten and create trouble for the federal government[1]. Stoner-Weiss (2000), however, questions the ability of the weakened and disintegrating central government to act adroitly and resolutely. She also demonstrates that control by the center over fiscal flows was an imprecise and clumsy instrument in curbing many regional challenges to central state governing capacity. Freinkman and Haney (1997) have shown that federal transfers to the regions do matter in explaining national economy expenditures funded by Russian regions, especially in explaining housing subsidies, but they were careful not to claim that the neediest regions have received the most in transfers. Stewart (1997) and Hanson (2000) have argued that federal government transfers to the regions – contrary to what many analysts claimed - are roughly compatible with the regional needs because they go mostly to the neediest regions. They believe, however, these transfers are too small and too thinly spread to make a difference. Popov (2001) has shown that net intergovernmental financial transfers are largely of the "Robin Hood" type, i.e., going mostly from rich to poor regions, but they are more than counterweighted by private business transfers going in the opposite direction.

Zhuravskaya (2000) provides evidence that in Russia, unlike in China, every time the municipalities are starting to earn greater revenues, the regional authorities tend to change rules

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[1] He argued that regions that voted against Yeltsin in 1991 and against pro-Yeltsin Russia's Choice bloc in December 1993, that issued early sovereignty declarations, and whose governors opposed Yeltsin publicly in his conflict with the parliament in September 1993, all seem to have received larger net transfers from the center in subsequent years. Also, Lavrov (cited in Martinez and Boex, 1999) and Triesman (1996) claimed that 21 ethnic republics of the RF enjoyed financial preferences, such as the retention of a higher share of tax proceeds, larger subsidies from the center, and single channel tax collection regimes.

about sharing taxes and providing transfers to municipalities in such a way as to appropriate these greater revenues for themselves. It is logical to expect that the federal government may exercise the same policy vis-à-vis the regions. Speckhard (2000) looked at the degree of the assertiveness of the particular regions, measured by their ability to gain privileges, including financial ones, from the center. He concluded that among other factors (size, economic potential, consolidation of the regional elite) the ability to deliver a majority vote for Yeltsin during 1996 presidential elections did provide particular regions with a bargaining chip in their relations with the center.

Finally, as many authors have observed (for instance, Solnick, 1999; Stoner-Weiss, 2000; Petrov, 2000), the federal approach to the regions in general and to intergovernmental transfers in particular did not stay the same throughout the 1990s. Whereas in the first half of the decade, following famous Yeltsin's appeal to the provinces – "take as much independence as you can swallow" – the balance of power in the Russian Federation shifted in favor of the regions, in the second half of the 1990s centralizing tendencies were evidently at play. Many observers considered Putin's rise to power (1999 parliamentary and 2000 presidential elections) as victory of poor regions over wealthy ones. The latter were united into a Primakov-Luzhkov "Fatherland- All Russia" electoral bloc that did not do well in the elections. Whether the center succeeded in recent years in centralizing the Federation is an open question, but there is no doubt that the center has tried to take a tougher stand on the regional autonomy.

2. The hypothesis: pacifying the troublemakers or rewarding the supporters?

If political factors influence patterns of intergovernmental financial flows, do they favor loyal to the center regions or "anti-center" regions, namely those that are involved in conflicts with the federal government? The Triesman hypothesis is that in the first half of the 1990s Moscow pacified the troublemakers in pretty much the same way as Vienna appeased ethnic and regional

claims within the Habsburg empire through tax concessions, new jobs, additional railway branch lines, and so on.

It is not enough to look only at *direct* financial transfers from the center to the regions – payments from the federal budget to the regional budgets. These *direct* transfers are only the visible part of the iceberg. The invisible part consists of tax revenues-sharing rules, which actually allow some regions to retain a greater than average portion of total revenues. *Total net* center-regional government financial flows should be calculated as the difference between the total revenues collected by all levels of government in the particular region and total outlays of regional and local authorities in this region. In this case the average region is certainly a donor vis-à-vis the federal government since federal taxes that are collected in the regions constitute the major source of revenues for the central government (although not the only source, since part of the revenues of the federal government, like custom duties and proceeds from privatization of federal property, are not disaggregated by regions). In 1996-98, in the period of financial stabilization, when prices were relatively stable, these annual net transfers from the regions to the center amounted to about 1000 rubles per capita (Predprinimatel'sky…, 1997; East West Institute, 1999), which was equivalent to about 8% of national GDP, or approximately equal to the average per capita income for 1.5 months (total revenues of the federal government amounted to 12% of GDP). The variations by regions, however, were huge: from over +7000R per capita in Moscow (national average per capita income for nearly 8 months) to -6000R per capita in Chukotka in the Far East (equivalent to nearly 7 monthly average per capita incomes). To put it differently, Moscow residents were paying "extras" to the federal budget equivalent to the average national per capita income for over half a year, whereas Chukotka residents were not paying anything to the central

budget, but were receiving net transfers equivalent to average national income per capita for over 6 months.

However, these net financial flows cannot be used without adjustment to measure the donor-recipient relationship between the federal government and the regions. Consider the same example of Moscow and Chukotka. Tax generating potential in Moscow is greater than in Chukotka because Moscow is wealthier and because industries that are located in Moscow generate more income. On the other hand, the cost of providing the standard basket of government services in Chukotka is higher than in Moscow – partly because the cost of living in Chukotka is higher and partly due to climatic and other conditions (for instance, more fuel is needed for heating schools, hospitals, etc.). Hence, both – total tax revenues collected in the region and expenditure of regional governments – have to be adjusted.

This paper uses the notion of ideal transfers per capita (ITcap), which are calculated as the difference between all tax receipts (federal and regional) per capita in Russia on average (TAXREVcap) adjusted for the index of tax potential of the particular region (ITP) and average Russian expenditure of regional governments per capita (RGEXPcap) adjusted for the index of budgetary expenditure (IBE):

$$ITcap = TAXREVcap * ITP - RGEXPcap * IBE$$

Defined in such a way, ideal transfers are the difference between taxes that the region is able to collect, given the objective conditions in this particular region, the average Russian level of tax rates and tax compliance, and expenditure that the regional government should make in order to ensure the provision of the average Russian level of public services to local inhabitants. To put it differently, ideal transfers guarantee complete equalization: every region is asked to contribute to the federal budget in line with its tax potential and every regions gets enough funds to maintain

public services at the average Russian level (i.e., if tax proceeds that could be collected in the region given its tax base are not enough, the region gets transfers from the center)[2].

The index of tax potential may be computed in various ways. One method is to take into account regional differences in gross regional product (GRP) per capita and in industrial structure (oil and gas industries generate more tax revenues than agriculture) – (see Batkibekov, Kadotchnikov, Lugovoy, Sinel'nikov, Trounin, 2000). Another method is to evaluate tax base in the region (value added for VAT, business profits for profit tax, personal income for personal income tax, alcohol and tobacco sales for excise taxes, etc.) and to multiply it by average national effective tax rate, i.e., the ratio of all tax proceeds to the tax base in the RF (Methodology, 2000). The first method is currently used by the Department of Finance of the RF to compute transfers to the regions from the Fund of Financial Support of the Regions (FFSR) – see (Minfin, 2001). Both methods yield results that are very consistent with the ranking of the regions by their GRP per capita; the current methodology used by the Russian Ministry of Finance to calculate transfers from FFSR for the year 2001 uses the ITP, which is highly correlated with the GRP per capita (R^2= 98%).

The index of budgetary expenditure (IBE) can also be computed in various ways. The most straightforward approach is to compare the cost of the basket of goods that represents the subsistence minimum, since it is assumed that regional differences in cost of provision of public goods are largely similar to regional variations in the cost of basic necessities. All other methods to compute the IBE necessarily take into account the cost of living index (subsistence minimum, cost of fuel, etc.), but also allow for other factors that may require higher/lower spending per capita by the regional governments aiming at providing public goods to the inhabitants of the region at a

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[2] This hypothetical complete equalization scheme could be likened to the realization of the communist principle "from each according to ability, to each according to needs". The needs in this case are defined as the average Russian standard of the provision of public goods by regional governments.

national average level. Such factors include climatic conditions, age structure of the population, the level of the development of infrastructure, share of urban population, etc. These factors affect all major categories of regional governments spending – from housing (housing is heavily subsidized from regional budgets and housing subsidies account for 20 to 50% of total regional government outlays) to education and health care, social assistance, public administration, and so forth. Currently, the computation of this official IBE is quite cumbersome and involves adjustments for federal standard of housing subsidies per 1 square meter of living space, the cost of living, the share of the population living in Far North and Arctic regions, the share of the population below the poverty line, transportation accessibility, the age structure of population, and other less important factors. This index is quite strongly correlated with the subsistence minimum.

To continue with the previous example of Moscow and Chukotka, for the calculation of the ideal transfers it is necessary to take into account that the tax potential (ITP) in both regions, which, for Moscow and Chukotka, is roughly 2 times higher than the Russian average, whereas the index of budgetary expenditure (IBE) for Moscow is around 1, and for Chukotka – from 4 to 8 (according to various calculations). That is to say, both Moscow and Chukotka have a capacity to generate two times more tax revenues per capita than Russia on average, but in Moscow one ruble of spending can deliver about the same amount of public goods as in RF on average, whereas in Chukotka the same amount of public goods can be purchased for 4-8 times as many.

The calculation of ideal transfers is shown in table 1. In 1997, both Moscow and Chukotka had a tax generating capacity of 7756 R per capita, but the maintenance of a national average standard for the provision of public goods required 3030R per capita in Moscow and 18180 in Chukotka. Hence, ideally Moscow was supposed to pay the federal budget 4726 R per capita (7756-3030), but in fact paid 8311 R, whereas Chukotka ideally was supposed to get 10424 R per

capita (7756-18180) from the center, but in fact received only 7596 R. The difference, which can be conceived of as Moscow's "overpayment" to the federal center (3555 R per capita) and Chukotka "under-financing" from the center (2828 R) – may or may not be related to political factors[3].

Table 1. **Approximate calculation of ideal transfers for 1997**

Region	ITP, approx. average of different estimates	Adjusted tax revenues, R per capita	IBE, approx. average of different estimates	Adjusted expenditure of regional governments, R per capita	Ideal net transfers from the region to the center, R per capita*	Actual net transfers from the region to the center, R per capita*	Difference between actual and ideal, R per capita
(1)	(2)	(3)=3878*(2)	(4)	(5)=3030*(4)	(6)=(3)-(5)	(7)	(8)=(7)-(6)
RF average	**1**	**3878**	**1**	**3030**	**848**	**1166**	**318**
Moscow	2	7756	1	3030	4726	8311	3585
Chukotka	2	7756	6	18180	-10424	-7596	2828

*Actual net transfers from the region to the center per capita for the RF on average (1166 R) are not equal to ideal transfers (858 R) because ideal transfers are computed with the exception of non-tax revenues (part of these non-tax revenues, like revenues from the privatization of federal property, are not divided by the region of origin).

In every federation there is a difference between actual and ideal net transfers, since complete equalization is normally not carried out and probably should not be carried out even from a purely theoretical point of view.[4] The inability of particular regions to provide the national average level of public services may be the result of poor infrastructure. In this case the federal government can try to stimulate the development of the regional infrastructure through shared projects (with the regional government) rather than compensating infrastructure inadequacies through non-conditional equalization payments. However, the point of this paper is to test whether

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[3]There are special factors, of course, especially for small regions, such as Chukotka (with a population of just over 70,000 in 2001). In December 2000, Roman Abramovich, the oil-aluminum "oligarch" was elected governor of Chukotskiy AO by 91% of the voters. The regional budget for 2001 includes $65 million from federal and local revenue sources. Abramovich promised to match that himself - through $35 million in personal income tax and $30 million for the Pole of Hope charity fund (Washington Post, March 2, 2001).

[4] There are also differences in fiscal potential and fiscal requirements within the regions – between counties and municipalities – and there are equalization schemes within regions. In 1999 the RF average ratio of budgetary capacity of richest and poorest municipalities in the regions was 14.4 before equalization and 4.8 after equalization (Obzor…, 2001, p. 138).

the difference between actual and ideal net transfers is influenced by political factors, in particular by center-regional relations. The hypothesis is that in the 1990s pro-Moscow oriented regions were paying less (or more) to the center (i.e., getting from the center more/less respectively) than they should.

3. Review of data and events

The data on net transfers per capita from the regions to the center are deflated using the official GDP price deflator, so that all transfers are expressed in 1997 prices. This makes it easy to compare them with previously calculated ideal transfers for 1997 (the ideal transfers for earlier years cannot be computed because of the lack of data). As fig.1 suggests, actual net financial flows were more or less consistent with the ideal transfers, especially in 1995-2001, when the R^2 of the linear equations linking actual and ideal transfers was always above 40% (the coefficients in these equations were highly statistically significant in all years).

Table 2 presents the correlation coefficients (R) for net financial transfers from the regions to the center. It is noteworthy that for all years actual transfers are pretty much correlated with the ideal transfers, no matter how they are calculated. But there are two obvious breaks in continuity – in 1995 and in 2000. Consider the chain correlation coefficients – that of the current year with the previous year – these are shown in the table in the shadowed cell on the diagonal line and tell the story of how much the pattern of transfers in the current year corresponds to the pattern of the previous year. All these coefficients are higher than 0.87, except for the 1995 and for 2000-01. Besides, 2000 actual transfers are less correlated with ideal transfers than actual transfers in any year in 1995-2000, and less correlated with the previous actual transfers (shadowed cells in the row for 2000) than actual transfers for every year since 1992. This implies there were changes in the patterns of financial flows in 1995 and 2000, although the real meaning of these changes,

especially that of 2000, is not crystal clear at a moment. It is obviously connected with two major reforms in inter-budgetary relations.

Fig. 1. Ideal transfers (Martinez, 1997) and actual transfers in 1997 prices in 1992-2001
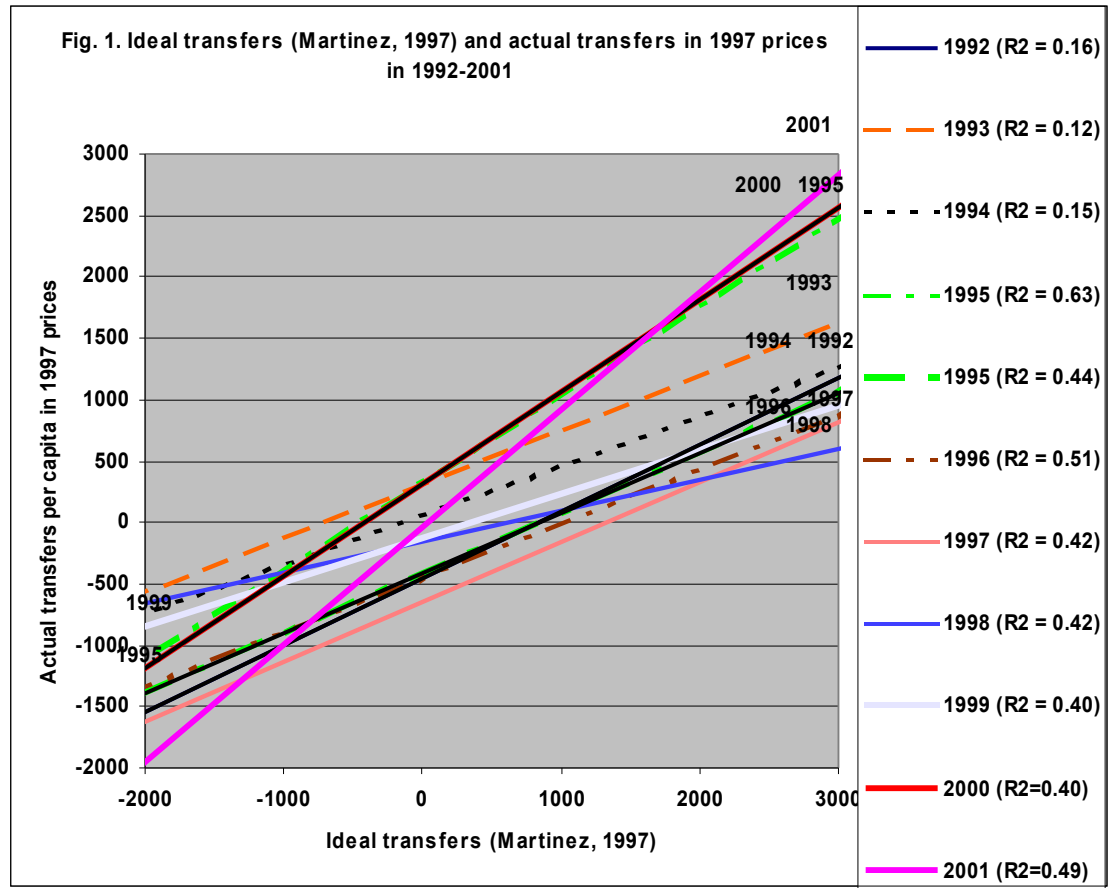
In 1994 the tax sharing procedures were unified and the Fund for Financial Support of the Regions (FFSR) was created: whereas previously financial relations between Moscow and the regions were of the type of pure "contractual federalism" (Heinemann-Gruder, 2002) and were based on the negotiated and *region-specific* tax-sharing procedures with and transfers from Moscow, in 1994 the first formula-based mechanism was introduced. The equalization formula, however, was based on *actual* tax collection and *actual* expenditure of regional governments for previous years and did not take into account either the tax *potential,* or budgetary *requirements*. Still it can be speculated that this was the major improvement of the previous procedure of

continuous bargaining and resulted in bringing the actual transfers more in line with ideal transfers because the correlation coefficients of actual transfers with the ideal transfers starting from 1995 improved dramatically as compared to 1992-94.

Table 2. Correlation matrix for actual per capita net financial transfers from regions to the center in 1997 prices in 1992-2001   (88 observations)

Net per capita transfers in 1997 prices	1992	1993	1994	1995*	1995 *	1996	1997	1998	1999	2000	2001	Ideal transfers 1997 (Mart)	Ideal transfers 1997 (Meth)
1992	1												
1993	0.87	1											
1994	0.92	0.96	1										
1995 *	0.81	0.79	0.77	1									
1995 *	0.55	0.43	0.51	0.80	1								
1996	0.58	0.45	0.51	0.83	0.96	1							
1997	0.60	0.49	0.54	0.84	0.95	0.96	1						
1998	0.50	0.43	0.49	0.74	0.92	0.93	0.94	1					
1999	0.54	0.43	0.49	0.78	0.95	0.95	0.97	0.96	1				
2000	0.33	0.20	0.32	0.58	0.59	0.59	0.57	0.57	0.54	1			
2001	0.45	0.40	0.39	0.71	0.68	0.74	0.71	0.66	0.74	0.18	1		
Ideal transfers 1997 (Martinez) **	0.41	0.34	0.39	0.79	0.67	0.71	0.65	0.65	0.64	0.63	0.70	1	
Ideal transfers 1997 (Methodology) **	0.46	0.39	0.40	0.83	0.70	0.78	0.74	0.71	0.73	0.51	0.82	0.94	1

*The first figure for 1995 is obtained using the official Minfin data, the second one – using the data published by the EWI (East-West Institute, 1999, 2000). The data for 1996-99 are from the EWI, for 2000-01 – from Minfin and MNS (Ministry of taxes and duties).
**The "Martinez" ideal transfers are computed with ITP = GRP per capita and IBE = subsistence minimum. The "Methodology" ideal transfers are computed as explained in (Methodology…, 2000) – see previous section.

In 1999-2000 another reform was carried out – this time the formula to calculate transfers to the regions from the FFSR was based on indices of tax potential and indices of budgetary expenditure and supposedly should have resulted in the streamlining the actual flow of transfers in such a way that they correspond even more to the ideal transfers. Nevertheless, the actual pattern

of transfers in 2000 and 2001 does not exhibit a closer link to the ideal transfers; on the contrary, the correlation coefficients with ideal transfers for the year 2000 are the worst ones in the whole period of 1995-2001, whereas for 2001 these correlation coefficients do not show considerable improvement and are pretty much in line with that of 1995-99 period (table 2). Another puzzle is that the pair wise correlation coefficients of actual 2000 transfers with the transfers for the other years are noticeably lower than the similar correlation of actual transfers for every other year of the preceding period and even for 2001. That is to say that in 2001, after the reform, actual transfers were more consistent with the pre-reform patterns of transfers than with the pattern of the year 2000 that obviously sticks out of the crowd. The correlation between actual 2001 transfers and 2000 transfers is the worst – only 18%. Here the puzzle is only formulated, the discussion is given in the next section after the regression analysis.

Pro- or anti-Moscow position of the particular regions can be measured by several indicators. The most straightforward measure is the share of the votes cast for Yeltsin in 1991 and in the second round of 1996 presidential elections and the ratio of votes given to democratic parties to the votes collected by leftist parties in the parliamentary elections of 1993, 1995 and 1999. The political position of the federal government in the period under consideration was to the right of the center, if the center is defined as the average political orientation of 89 regions of the RF. Therefore, the pro-democratic orientation of the electorate of the region was the one that generally pleased the federal center more than the pro-leftist orientation. Such a scheme is definitely a simplification, but basically a right one: the anecdotal evidence strongly suggests that the relationship of the regions of the "red belt" with Moscow was more tense than that of pro-democratic regions.

As table 3 suggests, political preferences of Russian voters in the regions were very stable during the last decade. Overall, there is only one serious and significant deviation from the dominant geographical pattern of voting in Russia in the 1990s and the early 2000s – the pro-Putin vote at 2000 presidential elections, but this is exactly the kind of exception that proves the rule. It is well known that Putin's phenomenon has to do more with political technology than with ideological preferences, that Putin's electorate includes people of different and even conflicting political preferences (Colton, McFaul, 2000). Even in the 2000 presidential election the geographical split between the ideologically oriented voters (that of Yabloko and that of communists) was very much in line with the previous years. It is only Putin's share of the votes that is not correlated with "ideological" voting patterns. It is also important to note that pro-democratic regions are usually richer than pro-leftist: the pro-democratic and pro-incumbent president vote, except for voting for Yeltsin in 1991 and for Putin in 2000, is quite correlated with the GRP per capita. So it may well be that the opposition regions are forced to pay more to the federal budget not because of their opposition per se, but because of their poor status (low importance) in the federation.

In addition, there are indices of tensions in the relationship between the regions and the center[5] and indices measuring the power of regional administrations, where higher values represent more bargaining power with the center[6]. Finally, there are dummy variables that were used for the

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[5] One index comes from RUIE (Predprinimatel'sky…, 1997). The other index is constructed by MFK Renaissance (Ponomareva, Zhuravskaya, 2000) and takes account of the frequency of public statements by the governor against the policies of the center, the extent to which regional laws and regulations violate federal laws, the level of support of the governor by the center at the last elections, and the existence of a bilateral treaty between the region and the center. These two indices of tensions are strongly correlated.

[6] One was computed by RUIE based on the average of estimates provided by experts (Predprinimatel'sky…, 1997). The other is provided by the Urban Institute based on the analysis of regional legislation and its violations of federal laws, federal elections results (pro- or against the center policies), the regional natural resource endowment and other relevant information (Ponomareva, Zhuravskaya, 2000). Once again, the two indices are positively correlated, although not as strongly as the indices of tensions with the center.

regression analysis, such as a capital city dummy (Moscow), AO dummy (for 11 autonomous regions – oblast'and okrug) and republic dummy (for 21 regions that are called republics). Formally, according to 1993 Constitution, all 89 regions of the RF have equal rights, but it may be that the remnants of the Soviet past (when the rights of republics, AOs and oblast's were different) still play a role in fiscal federalism.

Table 3. Correlation matrix for different measures of pro-Moscow voting at national presidential (1991, 1996, 2000) and parliamentary (1993, 1995, 1999) elections in the regions (for parliamentary elections – ratio of votes cast for democratic parties to the votes cast for leftist parties*) – 68 observations

ELECTIONS	% of votes cast for Yeltsin in 1991	Parl-1993	Parl-1995	% of votes cast for Yeltsin in 1996 (2nd round)	Parl-1999	2000-Yavlinsky/Zuganov*	% of votes cast for Putin in 2000	GRP per capita, 1996
% of votes cast for Yeltsin in 1991	1							
Parl-1993	0.42	1						
Parl-1995	0.47	0.85						
% of votes cast for Yeltsin in 1996 (2nd round)	0.37	0.79	0.78	1				
Parl-1999	0.50	0.84	0.86	0.84	1			
2000-Yavlinsky/Zuganov**	0.43	0.74	0.88	0.76	0.87	1		
% of votes cast for Putin in 2000	0.12	0.34	0.31	0.52	0.36	0.22	1	
GRP per capita, 1996	0.27	0.68	0.51	0.60	0.56	0.46	0.17	1

*Democratic parties – DVR/SPS and Yabloko; leftist parties – KPRF, Agrarians, Communists – Workers' Russia.
** Ratio of votes cast for Yavlinsky (Yabloko presidential candidate) to votes cast for Zuganov (communist candidate).
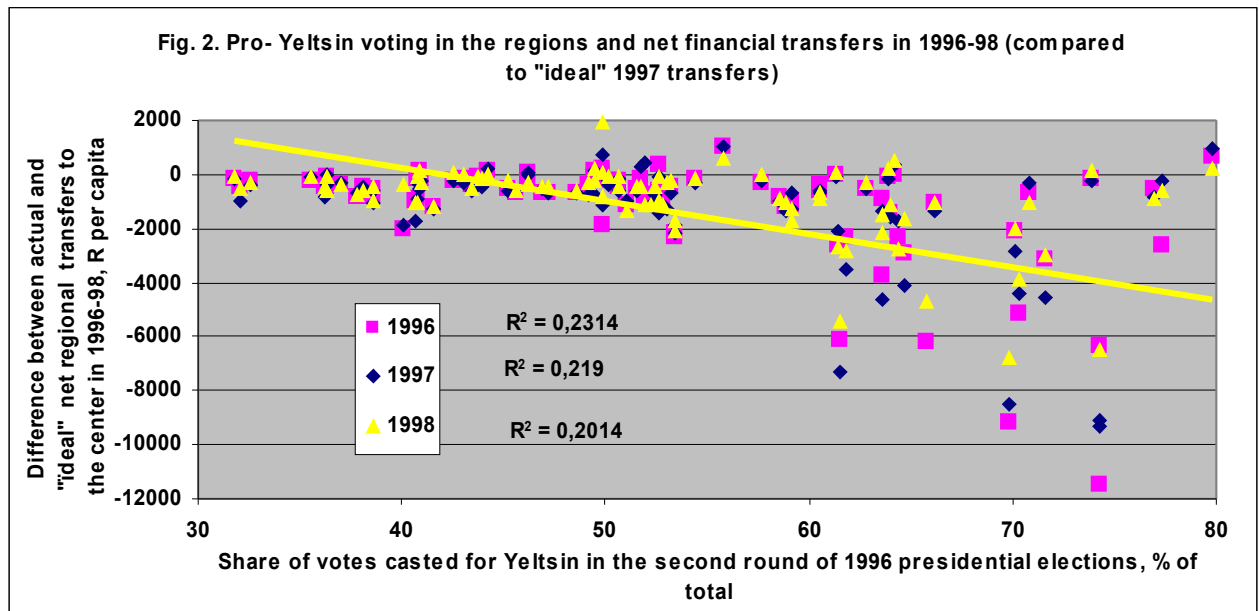
The general result of comparing actual transfers with ideal transfers is that the difference between them is negatively correlated with pro-Yeltsin and pro-federal government voting in the

regions, negatively correlated with the power of the regional administration and positively correlated with tensions between the region and the center. To put it differently, three political factors allowed the regions to reduce their transfers to the center: (a) voting in support of incumbents at presidential elections and in support of pro-Moscow parties in parliamentary elections, (b) greater bargaining power in relations with the center, and (c) lower tensions with the federal center. Pro-Moscow voting patterns and good relations with Moscow led to pecuniary benefits – they materialized into tangible monetary remuneration in the form of lower net transfers to the center or higher net transfers from the center as compared to "ideal" amounts (computed with the assumption of complete equalization). This result is very robust using various measures of fiscal capacity (ITP) and costs of provision of public goods (IBE), with one exception discussed later.

For example, the negative relationship between pro-Yeltsin voting patterns and transfers from the regions to the center can be observed in fig. 2: in every year - 1996, 1997 and 1998 – regions that supported Yeltsin in the 1996 presidential elections paid less than they should to the center or received more than they were entitled to from the center. It is noteworthy that there is virtually no relationship between actual (unadjusted) transfers and pro-Yeltsin voting.

Fig. 3 presents the data on linkages between voting patterns at 1993 parliamentary elections and the gap between actual transfers in 1997 prices and ideal transfers for 1997. The general relationship is only too obvious and can hardly be a coincidence. In virtually all cases the relationship is negative and statistically significant (other electoral results are not shown to save space) – the more the electorate in the regions supports pro-Moscow candidates, the less the region should pay to the center. Or, to put it more rigorously, the more votes are cast in the region for incumbents at presidential elections and for democratic parties in national parliamentary

elections, the smaller is the difference between what the region had actually paid to the center and what it had to pay according to the formula. In most cases this difference is negative because there is no complete equalization of abilities to provide public goods by the regional governments. However, while all regions pay less that they should have paid for complete equalization, pro-Moscow oriented regions pay even less. The co-operation with the Big Brother in Moscow definitely paid off, while opposition to the federal center was expensive in a very literal meaning of the word. Exceptions (1992 and 1999-2001) are discussed below.

Fig. 2. Pro- Yeltsin voting in the regions and net financial transfers in 1996-98 (compared to "ideal" 1997 transfers)

Empirical results: electoral politics and transfers

Regression results for net financial flows from regions to the center are reported in tables 4 – 7 and generally confirm the previous observations. In 1992 the pattern of transfers seem to have been that of pacifying the troublemakers – the more votes were cast for Yeltsin in 1991 presidential elections the more payments to the center the region was actually making even

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controlling for objective measure of financial contribution (ideal transfers) and for GRP per capita (the richer regions were paying less). In 1992 this pacifying pattern is statistically significant (table 4) – this provides the support for Triesman hypothesis of appeasing the opposition regions, although the correlation coefficients are very low (R^2 does not rise to over 29%). However, for 1993 transfers such variables as the share of votes cast for Yeltsin and the GRP per capita become insignificant, it is only ideal transfers that remain significant, and the explanatory power of the regression drops to a very low level (R^2 is only 16% and lower), which may suggest that there was a complete chaos in fiscal federalism at a time.

Fig. 3. Ratio of votes cast for Russia's Choice and Yabloko to the votes cast for communists and agrarians at 1993 parliamentary elections, %, and difference between actual (adjusted for inflation) and ideal transfers - trend lines
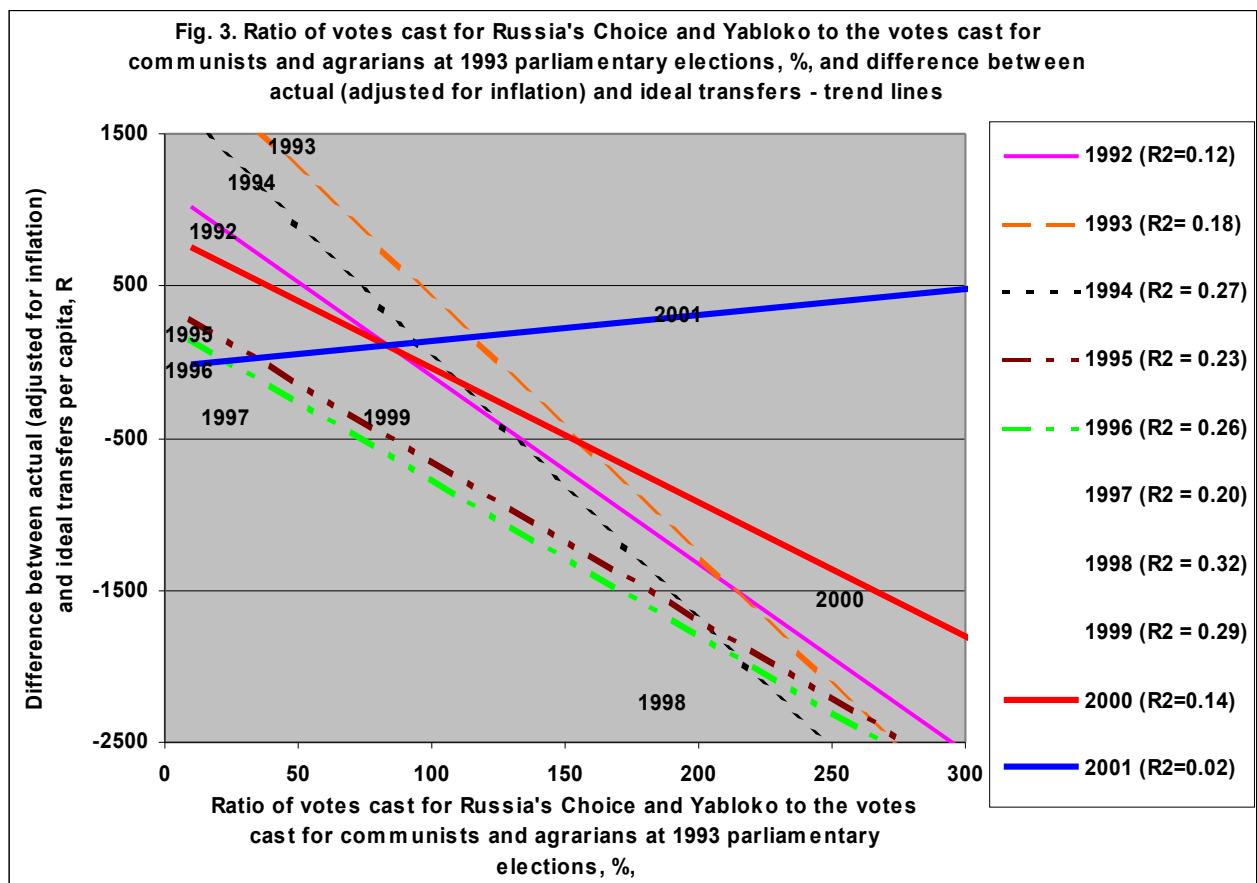
Table 4. Regression of actual net financial transfers from regions to the center in 1992-93 on ideal transfers and 1991 election results (T-statistics in brackets)

Dependent variable	Actual 1992 per capita transfers in 1997 prices, N=85	Actual 1992 per capita transfers in 1997 prices, N=85	Actual 1992 per capita transfers in 1997 prices, N=85	Actual 1993 per capita transfers in 1997 prices, N=85	Actual 1993 per capita transfers in 1997 prices, N=85	Actual 1993 per capita transfers in 1997 prices, N=85
Ideal transfers (Methodology)		0.55*** (4.1)	1.21*** (4.8)		0.46*** (3.4)	0.60** (2.2)
Ideal transfers (Martinez)	0.47*** (3.4)			0.39*** (2.8)		
Share of votes cast for Yeltsin in 1991	**83.62 * (1.7)**	**81.78* (1.7)**	**88.72* (1.9)**	**50.57 (1.0)**	**49.25 (0.3)**	**50.75 (1.0)**
GRP per capita in 1996, % of RF average			-34.05*** (-3.0)			-7.36 (-0.6)
Constant	-4714* (-1.8)	-4721* (-1.9)	-2831 (-1.1)	-2263 (-0.9)	-2277 (-0.4)	-1868 (-0.7)
Adjusted R^2, %	17	22	29	10	14	16

*, **, *** - Significant at 10%, 5% and 1% level respectively.

In 1994-95, however, the pattern of financial flows changes dramatically (table 5). First, the explanatory power of regression increases greatly since 1995 (from 26% to over 70%), and so does the significance of the coefficients of ideal transfers, suggesting that 1994 reform of financial flows was really efficient in bringing these flows more in line with the ideal pattern. Second, from 1994 the sign of coefficient of the variable characterizing the electoral results (ratio pro-democratic to pro-leftist votes at December 1993 parliamentary elections) becomes negative and the coefficient itself – statistically significant. The more the regions supported the leftist parties at the 1993 parliamentary elections and the less they supported the pro-democratic parties, the higher were their financial transfers to Moscow.

Table 5. Regression of actual net financial transfers from regions to the center in 1994-96 on ideal transfers and 1993 election results (T-statistics in brackets)

Dependent variable	Actual 1994 per capita transfers in 1997 prices, N=82	Actual 1995 per capita transfers in 1997 prices, N=82[+]	Actual 1995 per capita transfers in 1997 prices, EWI, N=82	Actual 1996 per capita transfers in 1997 prices, N=82
Ideal transfers (Methodology)				0.52*** (10.0)
Ideal transfers (Martinez)	0.69*** (5.5)	.86***(12.8)	0.68*** (9.8)	
1993 parliamentary elections - Democratic parties/leftist parties, %	**-11.83*** (-3.1)**	**-3.54* (-1.7)**	**-3.01* (-1.8)**	**-2.07 ** (-1.6)**
Ratio of income to subsistence minimum in 1998, %	Insignificant	Insignificant	9.38** (2.8)	9.76*** (3.7)
AO Dummy			-5332*** (-6.9)	-3258*** (-5.3)
Constant	14.81** (2.3)	816** (2.4)	-1278** (-2.3)	-2263 (-0.9)
Adjusted R^2, %	26	72	74	78

*, **, *** - Significant at 10%, 5% and 1% level respectively.
[+]Data in the previous columns (1994-95) are from Minfin; data in the following columns are from EWI.

It appears also that rich regions were paying more in 1995-96: the coefficient of the ratio of income to subsistence minimum (cost adjusted measure of living standards) was positive, suggesting that regions with higher living standards were paying more to the center. But for 1994 the inclusion of variables that measure living standards in the region (GRP per capita or ratio of income to subsistence minimum) does not change the results, and the coefficients of these variables turn out to be insignificant. To put it differently, opposition regions were forced to pay more not because they were mostly poor, but because they voted in a way that displeased the federal center.

In subsequent years, 1996-99, the described pattern of asymmetrical federalism was consolidated. The results for this period are consistent with 1994-95 pattern and are very stable (table 6). Regions that voted against Yeltsin at 1996 presidential elections, regions with high

tensions in relations with the center, poor regions and regions with no autonomous republic/orkrug status, as well as Moscow, had to pay more to the federal budget than others.

Table 6. Regression of actual net financial transfers from regions to the center in 1996-99 on ideal transfers and 1996 election results (T-statistics in brackets)

Dependent variable	Actual 1996 per capita transfers in 1997 prices, N=88	Actual 1997 per capita transfers in 1997 prices, N=88	Actual 1998 per capita transfers in 1997 prices, N=88	Actual 1999 per capita transfers in 1997 prices, N=88
Ideal transfers (Methodology)	0.80*** (12.3)	0.88*** (10.3)	0.44*** (10.3)	0.71*** (11.9)
1996 presidential elections -% of votes cast for Yeltsin in the 2nd round	**-24.00* (-1.8)**	**-39.64** (-2.2)**	**-16.08* (-1.7)**	**-21.31* (-1.7)**
GRP per capita in 1996, % of RF average	-13.26*** (-4.2)	-11.49*** (-2.7)	-6.88*** (-3.3)	-11.73*** (-4.0)
AO Dummy	-2024*** (-4.3)	-2974*** (-4.8)	-1406*** (-4.6)	-2509*** (-5.8)
Moscow dummy	3239** (2.4)	4721*** (2.7)	5368*** (6.1)	4094*** (3.3)
Index of tensions, 1996, RUIE	322.26* (1.9)	499.22** (2.2)	85.81 (1.3)[+]	292.17* (1.8)[+]
Constant	1057(1.5)	1178 (1.3)	8 92**(2.0)	1210* (1.9)
Adjusted R^2, %	77	73	75	77

*, **, *** - Significant at 10%, 5% and 1% level respectively.
[+]Index of tensions is from MFK Renaissance.

Finally, the story of the Putin's period, 2000-01, is that of the complete change in the direction of transfers in the year 2000 and the surprising return to the previous patterns in the year 2001 (table 7). In 2000 the goodness of fit declines markedly, as well as the T-statistics for ideal transfers coefficients, (still significant, but much less than before and after), whereas the sign of coefficient of election variable changes from negative to positive. Was it the result of 1999-2000 fiscal federalism reform that introduced the new formula based on objective measures of fiscal capacity and budgetary requirements? Strictly speaking, the introduction of the precise formula should have resulted in the opposite developments – in the improvement of the explanatory power of the regression and in the increase of significance of the ideal transfers coefficient, whereas the

voting behavior of the regions should become insignificant. The reason that this did not happen is due to the new and peculiar way of computing the IBE: the latter initially, for the year 2000, was calculated taking into account many more factors than the cost of living (this changed the pattern of transfers dramatically), whereas in 2001 the IBEs for the regions were recalculated using the "new" objective data, so that the pattern of transfers in 2001 returned to that of previous years and has virtually nothing in common with the pattern of 2000.

Table 7. Regression of actual net financial transfers from regions to the center in 2000-01 on ideal transfers and 1999-2000 election results (T-statistics in brackets)

Dependent variable	Actual 2000 per capita transfers in 1997 prices, N=85	Actual 2001 per capita transfers in 1997 prices, N=85	Actual 2001 per capita transfers in 1997 prices, N=86	Actual 2001 per capita transfers in 1997 prices, N=86
Ideal transfers (Methodology)	1.14(5.7)	1.32 (15.6)	1.25 (13.5)	1.27 (13.2)
1999 parliamentary elections–votes for democratic parties/votes for leftist parties	**42.02*** (4.2)**	**-16.36** (-2.3)**		
% of votes for Putin at 2000 presidential elections			**-16.30 (-0.4)**	
Presidential elections 2000-votes for Yavlinsky/votes for Zuganov				**-16.11 (-0.7)**
GRP per capita in 1996, % of RF average	-38.97*** (-4.1)	Insignificant	Insignificant	Insignificant
AO Dummy	-2024*** (-4.3)	-4834*** (-4.0)	-3599*** (-2.7)	-3649*** (-2.8)
Constant	701(0.8)	788 (1.5)	751 (0.4)	141 (0.8)
Adjusted R^2, %	41	75	70	70

*, **, *** - Significant at 10%, 5% and 1% level respectively.

As was already mentioned, the official IBE is computed with the greatest number of adjustments – not only for the cost of living, but also for housing subsidies, share of the population living in Far North and Arctic regions, share of the population below the poverty line, transportation accessibility, age structure of population, and other factors. Unfortunately, due to

the lack of data, it is impossible to determine precisely what explains the difference between the official IBE and other measures of adjustment of budgetary spending. But it is possible to show that both – ideal transfers computed with official ITP and IBE, and the difference between official and unofficial IBE - are correlated with the actual pattern of transfers in 1996-96 and with the share of votes cast for Yeltsin in 1996. That is to say, the official IBE incorporated the influence of political factors that alter federal-regional financial flows, so it is by no means surprising that ideal official transfers (computed with official IBE) are no longer correlated with political factors. To cite one example, in all 7 regions where official IBE was over 400% of the RF average (Nenetsky AO, Taimyrsky AO, Evenkiysky AO, Sakha Republic, Chukotsky AO, Koryaksky AO, and Magadan oblast') the share of votes given to Yeltsin in the second round of 1996 presidential elections was higher than the national average, 62 to 74% against 54%. True, these are all Northern, Siberian and Far East regions with the high cost of living. But the other "expensive" regions (many of them are immediate neighbors of highest official IBE regions, but with less impressive pro-Yeltsin voting records) were assigned substantially lower official IBEs.

It is quite obvious that the ideal transfers computed with the official IBE are much closer to the actual transfers in 1996-98 than the ideal transfers computed with all other combinations of ITP and IBE, including official ITP for 2001 budget. It is easy to see this relationship from table 8, which reports the correlation coefficients for actual and ideal transfers calculated using various measures: if ideal transfers are computed with official IBE for 2001 RF budget (Minfin, 2001), they are noticeably more strongly correlated with the actual transfers in 1996-98.

Table 8. Correlation between actual net transfers from regions to the center in 1996-98 and different measures of ideal transfers

VARIABLES	Ideal transfers, ITP= GRP/cap, IBE= subs.min.	Ideal transfers, ITP=GRP/ cap+ind. Structure, IBE=Met (2000)	Ideal transfers, ITP=tax base* average tax rate, IBE= Met (2000)	Ideal transfers, ITP =GRP/cap +ind.struc- ture, IBE= subs. Min.	Ideal transfers, ITP= minfin 1998, IBE=subs. min.	Ideal transfers, ITP, IBE= minfin 1998
Actual net transfers, 1996	0.7728	0.7201	0.7863	0.7627	0.7462	**0.9116**
Actual net transfers, 1997	0.7724	0.6752	0.7632	0.7186	0.7459	**0.9270**
Actual net transfers, 1998	0.7250	0.6674	0.7266	0.7100	0.6861	**0.8605**

Table 9 summarizes the regression results for the variables explaining official ideal transfers and official IBE. It turns out that official ideal transfers (equations 1-3), after controlling for hypothetical ideal transfers computed with simple ITP and IBE, depend positively on the actual pattern of transfers in 1998 and negatively on the pro-bYeltsin vote, Moscow and AO dummies. In other words, official transfers for the 2001 budget were computed in such a way that they benefited Moscow, AOs and regions that voted for Yeltsin - those regions were required to pay less to the center. On the other hand, the newly computed official transfers disfavored regions that were paying a lot to the center previously, i.e. they were brought more in line with actual patterns of transfers in 1998.

This effect of the "streamlining" of the official transfers to bring them closer to the actual patterns of financial flows that existed previously and to make sure they are favorable for political supporters is due mostly to the newly computed IBEs, since newly computed ITPs remained quite in line with the objective measures of tax capacity. In fact, as equation 4 suggests, the difference between the officially computed IBE and the IBE based on the cost of subsistence minimum depends positively on pro-Yeltsin vote, Moscow and AO dummies and negatively – on the actual

transfers in 1998. That is, Moscow, AOs and pro-Yeltsin voting regions were assigned higher IBE

(to make sure they could leave more tax revenues in the region for the financing of their own

regional spending and to transfer less funds to the center). On the contrary, the more a region was

paying to the center before, in 1998, the lower the IBE was established for this region, presumably

to make sure the region continued to pay as much as it had previously[7].

Table 9. Regression of ideal transfers computed with official ITP and IBE and of official IBE on actual patterns of transfers in 1998 and on voting patterns (T-statistics in brackets)

Dependent variables:
- **Equations 1-3 – ideal transfers computed with official ITP and IBE**
- **Equation 4 – difference between the official IBE and IBE based on subsistence minimum**

Variables / equations, number of observations	1, N=88	2, N=88	3, N=88	4, N=88
Ideal transfers, ITP=GRP/cap, IBE= subs.min.	1.0*** (8.3)			
Ideal transfers, ITP=tax base* average tax rate, IBE= Met(2000)		0.7*** (8.2)	0.7*** (7.2)	
Actual net transfers in 1998	1.7*** (8.3)	1.6*** (8.1)	2.1*** (9.6)	-0.03*** (-7.2)
Pro-Yeltsin vote in 1996 pres. elections	-60.9*** (-2.9)	-70.3*** (-3.2)	-29.6* (-1.7)	2.0*** (3.3)
AO dummy			-1942** (-2.7)	171.0*** (8.0)
Moscow dummy			-14586*** (-6.7)	123.1* (1.7)
Constant	1972* (1.7)	1887 (1.6)	77.6 (0.1)	-75.2** (-2.4)
Adjusted R^2, %	85	85	91	63

*, **, *** - Significant at 10%, 5% and 1% level respectively.

To summarize, there is a clear evidence that the actual pattern of net financial transfers

between the regions and the center in the 1990s was only partly determined by objective indicators

of tax capacity and costs of providing public goods. Controlling for these objective indicators, it

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[7] The anecdotal evidence suggests that in 2000 a number of Moscow-based consultant agencies were hired by the regions in order to collect evidence that the IBEs computed for these regions initially are too low and need to be adjusted upwards.

turns out that fiscal flows were favoring AOs, regions voting in a pro-center way, regions with more bargaining power and with less tensions with the center. It also appears that the indices of budgetary expenditure for the 2001 RF budget were computed in such a way as to incorporate these actual patterns of transfers, i.e. to make sure that there is no need to alter the existing pattern of financial flows drastically. Therefore, the actual picture of financial flows in the federation in 2001 resembles that of 1994-99 more than that of 2000. *Plus ca change, plus c'est la meme chose?*

Although the pattern of financial transfers is determined by the results of the *previous* elections, it may well be that there is a endogeneity problem because the outcomes of different parliamentary and presidential elections in the 1991-2000 in the regions are closely correlated (table 3). To check whether there is a simultaneity (not only election outcomes influence transfers, but also transfers determine election results, i.e. regions that are forced to pay more to the center are voting against the pro-Kremlin parties in the protest) we ran a Hausman test, which failed to reject the simultaneity hypothesis. The search for instrumental variables did not produce any promising instruments for explaining the voting patterns for all elections (1991, 1993, 1995, 1996, 1999, 2000), but it has been possible to show that the voting patterns predicted on the basis of previous elections did not influence actual transfers, whereas the error terms (residuals from equations predicting the election results) were always statistically significant[8]. So, in fact, what really matters for fiscal intergovernmental transfers (after controlling for ideal transfers) is not so much the results of the previous elections, but the change in these results as compared to the earlier elections.

The recently conducted research on voting patterns in 4 regions of Russia (survey of several hundred individuals) confirms that fiscal intergovernmental transfers do not influence the

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[8] The results are not reported here, but are available from the author.

voting behavior (Debardeleben, 2003). Even though the voters themselves believe that they prefer to vote for candidates and parties that would ease the burden of financial transfers to the center, and even though they believe that the best way to do it is to co-operate with the federal authorities rather than to confront them, in reality their votes are determined by such factors as personal characteristics (age, etc.) and rather stable political preferences (attitudes towards democracy, market economy, war in Chechnya, etc.), whereas their views on fiscal federalism are not statistically significant. Russian voters, to put it differently, vote with their heart, rather than with their purse; ideological orientation is more important for them than the prospect of immediate pecuniary benefits, whereas this ideological orientation itself is rather stable.

4. Concluding observations and implications for future research

The main point of the paper was to identify the bias in the Russian style fiscal federalism. The previous research provided evidence that there is no major bias (i.e. Russian fiscal federalism is symmetrical) or that there was a bias in favor of regions that oppose the federal center, i.e. the federal government is pacifying the troublemakers. This paper contains evidence to the contrary: rather than appeasing the opponents, the federal center seems to punish them financially. Regions that voted for leaders and parties that challenged the federal government and that had more tensions with Moscow tended to get less funds from the center in the 1990s and the early 2000s with the possible exception of 1992-93[9].

The period of 1992-93 is generally believed to be the period of decentralization and it may well be that the trouble-making regions were treated at that time in an appeasing rather than in an oppressive way. As was shown, there is no strong evidence that fiscal federalism in these early

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[9] There are two reasons, why these conclusions differ from those reached in other studies. For one thing, they are based on examining *total net* financial flows between the regions and the center, not only particular elements of these flows, like transfers from the federal budget to the regions or the share of total tax revenues retained by the region. The other reason is that net financial flows are adjusted for the objective regional differences in tax generating capacity and in costs of providing public services.

years was skewed in either direction. It is remarkable, however, that the oppressive pattern of dealing with "anti-center" regions emerged as early as in 1994 – right after the centralization drive that followed the forceful dissolution of the parliament by the president in October 1993. It is no less remarkable that the attempt to change the existing oppressive system in 2000 undertaken by Putin administration in the framework of the general campaign to curb the power of the rich regions and to trim their financial resources in favor of poorer regions was very short lived and did not produce a more fair distribution of financial resources. It led first, in 2000, to unexpected and controversial results (the richer regions in fact got some concessions), but then, in 2001, the pre-2000 pattern of transfers was restored. The calculation of official transfers for 2001 federal budget was carried out in such a way that the pattern of transfers that existed in the 1990s was institutionalized: the official indices of budgetary spending (used to account for the uneven budgetary requirements of the regions) absorbed a considerable portion of variations in transfers caused by political factors.

This is not to say that nothing changed in 2000-2001 in Russian system of fiscal federalism. The share of the federal government in revenues and expenditure of consolidated budget increased markedly in 1997-2001 (Obzor…, 2001; OECD, 2002). More important, taxing powers were greatly centralized: in 2002 over 70% of tax revenues of the consolidated budget came from taxes which were established at the federal level (both in terms of tax rate and tax base), so that the regional governments became extremely dependent on Moscow for financing their expenditure. In addition, the relative size of inter-budgetary transfers increased nearly two times –from 1.3% in 1999 to 2.54% in 2001 as a % of GDP (i.e. 18% of expenditure of regional and local budgets). However, this unprecedented centralization of national finances did not lead to

the elimination of political biases in fiscal federalism and did not alter the asymmetries that existed before the reform.

There are at least three implications for future research on fiscal federalism. **First**, it is quite understandable that it is impossible to change the existing asymmetrical pattern of financial flows overnight because of the political interests involved. The gradual approach to symmetry may be the only feasible solution. However, the adjustment of the coefficients used in the calculation of transfers in such a way as to make the asymmetrical arrangements look symmetrical is probably the worst possible scenario, since in this case the mechanisms of fiscal federalism become non-transparent and misleading. The simplification of the current transfer calculation scheme, especially of the computation of IBEs, even though it may lead to the large discrepancies between actual and ideal transfers, is definitely a preferable solution.

Second, until now the existing pattern of asymmetrical fiscal transfers in Russia proved to be very stable and robust in two senses. For one thing, the pattern of transfers and the pattern of voting was characterized by a lot of inertia: even though the opposition regions were "underpaid and overtaxed" by the federal center that tried to punish them for their opposition stand , they did not change their political orientation. The geographical pattern of political preferences of Russian electorate in terms of left-right divide remained very much the same all over the 1990s and in the early 2000s – more prosperous Northern resource regions, Moscow and St.-Peterburg retained their liberal, democratic and pro-reform orientation, whereas poorer regions, usually Southern, with large agricultural and heavy engineering sectors voted mainly for Communists and leftist/nationalist opposition parties. This may suggest that the Russians, very much like voters in other countries, tend to vote with their heart rather than with their purse – even faced with the consequences of the declining regional government spending on public goods as a result of their

opposition vote, they still stay loyal to their party. Hence, even from the point of view of the central government the whole strategy of asymmetrical federalism that implies the financial punishment of the troublemakers can be put into question.

For the other thing, the attempts to change the pattern of financial transfers by Putin administration in 2000 so far proved to be futile. Not only the pattern of voting, but the existing pattern of transfers as well exhibited a lot of inertia. Even though the formula for the distribution of transfers from the FFSR was established in 1999 and the new pattern of transfers in 2000 was really very different from the previous years, in 2001 the financial flows between the regions and the center returned to their prevailing pattern of the 1990s. Such a shift theoretically unthinkable in the presence of the formula specifying the exact amounts of transfers became possible mainly due to the recalculation of the indices of budgetary spending, which was carried out under the pressure from the disadvantaged regions. To use the Russian proverb, the asymmetries of the fiscal federalism were pushed out through the door, but nevertheless came back through the window.

The story is only too familiar, it was observed more than once in other areas of the economy that were selected for reform experiments: carefully designed and allegedly flawless reforms undertaken with best intentions very often produced unexpected and controversial results. Thus, macroeconomic exchange rate based stabilization of 1995-98 resulted in demonetization and barterization of the Russian economy and ended up in a currency crises of 1998. Similarly, the highly praised 1998 bankruptcy legislation that was designed to facilitate restructuring and gave more rights to the creditors than bankruptcy laws in Western countries, resulted in the capture of institution of bankruptcy by the regional governments.

And finally, **third**, Russian fiscal federalism presents a challenge for the theoretical research. The asymmetries of Russian federalism are of a different type as compared to Austro-Hungary. Whereas in the latter the center was retreating, giving more funds and rights to the opposing provinces, in Russia the center is advancing, punishing the opponents and rewarding the supporters. Contrary to the gentlemen-type "balance of power" and "art of possible" center-regional diplomacy of the Habsburg empire, the Russian federal government of the late 1990s was suppressing the opposing regions with the iron fist without the velvet glove.

If asymmetrical federalism (skewed in favor of benefiting regions that support the center) is regarded as an unstable equilibrium, it is conceivable that it could evolve into one of the three types of more stable equilibrium: (1) *authoritarian symmetrical federalism* resulting from the success of the center in undermining opposing regional governments (once the central government has ousted trouble-making authorities in the regions and replaced them with more loyal administrations, it stops their underfinancing); (2) *democratic symmetrical federalism* resulting from the abandonment by the center of the preferential policies towards particular regions; (3) *loosening of the federation* up to the point of the break up resulting from the inability of the center to impose its will on the opposing regions. The question, of course, is under which particular conditions each of the three outcomes becomes more or less probable.

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